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MANUFACTURERS HANOVER

Financial Digest

Volume XXV, Number 2 Friday, January 15, 1988

Analysis of Business Trends Plus Selected Financial Indicators

Is The Buck Bouncing Back?

Among the more persistent problems plaguing the financial markets both here and abroad are the seeming intractability of the U.S. trade deficit, and the negative effects of this huge red-ink total on the dollar's external value. This linkage was dramatically demonstrated one more time following the announcement of the October trade balance numbers in early December. With the trade deficit widening to a monthly record of $17.6 billion, the dollar subsequently nosedived over the remainder of the month, sliding to record lows against most major currencies. Even a renewed commitment by the G-7 industrial countries late last month to foster currency stability through foreign exchange market intervention and policy coordination was shrugged off by the markets, and the dollar ended the year on the ropes, ready to test new lows in early 1988.

But despite the dominant strain of bearish sentiment overhanging the foreign exchange markets, widespread expectations of further dollar weakness have so far failed to materialize. For one thing, the resolve of the central banks to mount a dollar defense, and back up their words with dollar buying deeds, was generally underestimated. During the first week of this year, major central banks intervened aggressively in the foreign exchange markets worldwide, buying perhaps as much as $4 billion in the open markets. This undertaking not only pushed the dollar's external value decidedly higher, up some six percent against the yen and nearly five percent versus the Deutschemark during the first five trading days of 1988, but also tempered the dollar selling enthusiasm of currency traders and speculators worldwide. For another, prospects for a sizable narrowing of the trade deficit in coming months gained a fair degree of credence in early January, a development which also tended to underpin the dollar.

The "Real" Trade Balance Is Improving

While central bank intervention can shore up the dollar temporarily, the fact remains that its longer-term fate will hinge on the pace at which the trade deficit either narrows or widens. This is why the trade statistics are now so closely watched. And, although hefty monthly trade deficits persist, there are actually several signs suggesting that the U.S. trade picture is improving, and that the dollar, rather than perched at the edge of a precipice, may be consolidating around a bottom at or near present levels.

Unfortunately, the extent of the progress in trimming the now $175 billion trade deficit, as measured in current dollars, is being masked by a combination of rising import prices in general, petroleum prices in particular and the ballooning of the trade deficit with the newly industrializing East Asian countries—Taiwan, South Korea, Hong Kong, and Singapore. But if one looks behind the current dollar numbers, at the inflation-adjusted or so-called volume statistics, it appears that the deterioration of the trade balance has not only stopped, but is in remission.

Between the third quarter of 1986 and the third quarter of 1987, the latest "real" trade data available, export volumes increased sharply while real imports have stood virtually still. Inflation-adjusted exports are up by 17½ percent, while import volumes have increased by just three percent. What is more, the inflation-adjusted trade deficit, excluding petroleum, peaked in the third quarter of 1986, and has since narrowed by some 30 percent.

But, with import price increases far outpacing export price increases, this volume progress has been masked. During the 12 months ending in September, import prices rose by better than 12 percent while export prices increased by less than 4½ percent. Rising oil prices were a principal culprit behind the import price hikes, as was the depreciation of the dollar during this period. For while the descent of the dollar in the foreign exchange markets has enhanced the price attractiveness of U.S. products overseas, it has also lifted the dollar price of imported products.

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Exports Soar While Imports Slow

However, even in current dollar terms, there are signs of improvement, especially on the export side of the ledger, witness the 9½ percent surge in exports in November. Combined with a six percent drop in imports, this performance cut November's trade deficit to $13.2 billion from $17.6 billion in the previous month. However, the deficit widened in the first 11 months of 1987 to $159 billion from $153.6 billion in the same period of 1986.

It is on the import side that the U.S. trade deficit seems most intractable. It appears that as long as the economy continues to expand, so does the appetite for foreign goods, particularly from East Asia. The growing deficit with the newly industrializing countries (NICs) of East Asia—Taiwan, Korea, Hong Kong, and Singapore—is a major obstacle to rapid trade balance improvement. The deficit with these countries soared to over $35 billion during the first 11 months of this year, accounting for almost one quarter of our global trade deficit—compared with about 8½ percent at the beginning of this decade.

Short Term Paper Outstanding

(Millions of Dollars)

Time Deposits of $100,000 or more Weekly Reporting Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/30/87)	174,082	+ 353	+ 18,088
New York City (1/6/88)	37,226	– 352	+ 1,591
Commercial Paper (1/6/88)	376,595	+19,083	+ 44,532

Bank Loans

(Millions of Dollars)

	Commercial and Industrial Loans		
Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/30/87)	280,163	+ 1,903	–11,559
New York City (1/6/88)	59,575	+ 696	– 7,913

	Total Loans and Leases Gross Adjusted		
	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (12/30/87)	809,802	+ 2,692	+ 7,697
New York City (1/6/88)	175,085	+ 2,286	+ 161

Financial Markets

	Friday 1/15/88	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	6.04%	– .01	+ .56
180-Day Bills†	6.55	– .21	+ .97
Longest Bills†	6.95	– .23	+ 1.28
Recent Issues:			
7⅞s 12/31/89	7.56	– .30	
8¼s 12/31/91	7.97	– .37	
8⅞s 11/15/97	8.59	– .40	
8⅞s 8/15/17	8.77	– .38	
Municipals:			
Bond Buyer–20 Bond Index* (1/14/88)	8.10%	+ .27	+ 1.45
Blue List Total ($ Million)	$ 783	– $103	–$ 953
30-Day Visible Supply ($ Million)	$1,547	+ $331	–$1,655
Total	$2,330	+ $228	–$2,608
Corporates:			
Moody's Aa Composite (1/14/88)	10.21%	+ .04	+ 1.37
30-Day Visible Supply ($ Million)	$6,033	+ $ 25	+$3,868
Stocks:			
Dow-Jones Averages:			
Industrials	1,956.07	+ 44.76	– 120.56
Transportation	756.00	+ 11.00	– 116.21
Utilities	178.40	– 3.32	– 44.42
65 Stocks	721.81	+ 10.45	– 80.57
N.Y.S.E. Composite Index	141.16	+ 4.13	– 11.05
N.Y.S.E. Avg. Daily Vol. for Week (000's)	163,706	– 23,039	– 44,452

*34% Taxable equivalent 12.27%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 1/15/88	Week Ago
Overnight	6.13%	6.63%
1 month	6.94	7.00
3 month	7.13	7.25
6 month	7.25	7.44
1 year	7.69	7.81
EURODOLLAR BONDS		
Average Yield		
Medium Term (5 yrs.)	9.18%	9.18%
Long Term (10 yrs.)	10.12	10.12

FOREIGN EXCHANGE SPOT RATES New York Opening (1/15/88)	Currency Per U.S. $	Week Ago
Canada	1.2896	1.2865
France	5.5350	5.5950
Germany	1.6695	1.6545
Italy	1226.00	1218.00
Japan	129.00	129.87
Mexico	2207.00	2204.00
Switzerland	1.3695	1.3540
U.K.*	1.7840	1.8020

*U.S. $ per U.K. pound

MH TRADE-WEIGHTED DOLLAR (1/15/88) (Adjusted for Inflation)	Change Since Week Ago	Change Since 2/27/85
	+0.3%	–1.9%

What is more, until recently, the NICs have kept their currencies closely tied to the U.S. dollar. This has limited the appreciation of their currencies versus the slumping dollar, enhancing their relative competitive edge in the United States market. For this reason, the dollar's trade-weighted depreciation since February 1985 against the currencies of our major trading partners is much less pronounced when the NICs are included than when they are not.

As long as consumption exceeds production, the trade deficit will remain sizable. To some extent, it is a reflection of the vigor of the U.S. economy and suggests that domestic demand must be dampened if there is to be a sustained narrowing of the trade deficit. However, it may not be too much longer before this occurs. With growth of consumer spending in real terms already falling, and the dollar drop in the foreign exchange markets likely to dampen spending on more costly imports even more, the worst could be just about over for the U.S. trade deficit in both current dollar and real terms. If so, the dollar's fortunes could improve as well. ■

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 1/13/88	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	227.889	– 3.004	+14.941
Loans to Depository Inst.	.981	– 1.927	+ .283
Float	2.719	+ 1.513	+ 1.768
Total Reserve Bank Credit	247.116	– 4.035	+15.672
Treasury Deposits with Federal Reserve Banks	3.871	– 1.160	– 2.088
Currency in Circulation	227.825	– 2.086	+16.633
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	204.386	+ 2.887	+40.780
	1/13/88		
Member Bank Reserves:			
Total Reserves Held	61.631	+ 2.670	+ 1.431
Excess (Deficiency)	1.156	+ .319	+ .311
Net Borrowed Reserves	.304	+ .786	+ .859
		% Change Since 3 Months Ago*	% Change Since Year Ago
Monetary Aggregates †			
M1 (1/4/88)	756.0	– 0.4‡	+ 2.3‡
M2 (December '87)	2,897.1	+ 2.9	+ 3.4
M3 (December '87)	3,665.4	+ 4.8	+ 4.9
Domestic Nonfinancial Debt (3rd Q'87)	8,139.1	+ 7.6	+ 10.0

†Seasonally adjusted. * Seasonally adjusted annual rate. ‡ Four-week moving average.

New York Money Market

Offering Rates 1/15/88	3 Months	6 Months	1 Year
‡U.S. Treasury Bills	5.91%	6.29%	6.55%
* Federal Agencies	6.65	6.80	6.90
* Municipal Notes—High Grade (34% Taxable Equivalent)	6.06	6.67	7.20
Negotiable Time CDs Manufacturers Hanover	Rates By Arrangement		
* Secondary Market—Prime	6.95	7.15	7.50

‡Finance Company Paper—Prime

5- 14 days	6.55%
15- 29 days	6.63
30- 59 days	6.70
60- 89 days	6.78
90-179 days	6.88
180-239 days	6.90
240-270 days	6.90

‡* Bankers' Acceptances

Feb.	6.70%
Mar.	6.70
Apr.	6.75
May	6.90
Jun.	6.90
Jul.	6.95

‡Industrial Paper—Prime

30- 89 days	6.78%
90-120 days	6.88

†Federal Funds Effective Rate 6.80%

‡Discount basis. *Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross National Product (Current Dollars)*	3rd Q'87	$ 4,524	$ 4,445	$ 4,266
Gross National Product (1982 Dollars)*	3rd Q'87	$ 3,836	$ 3,795	$ 3,718
Percent Change, Annual Rate	3rd Q'87	4.3	2.5	1.4
Change in Consumer Prices*	Nov '87	3.6%	4.8%	2.4%
Change in Producer Prices*	Dec '87n	– 3.6%	0.0%	1.2%
Civilian Employment (Thousands of Persons) †	Dec '87n	113,744	113,504r	110,657r
Unemployment as % of Civilian Labor Force†	Dec '87n	5.8%	5.9%	6.7%
Personal Income*	Nov '87	$ 3,834	$ 3,851	$ 3,590
Leading Indicators Composite Index (1967=100)†	Nov '87	190.2	193.5	182.7
Industrial Production Index (1977=100) †	Dec '87n	133.3	133.1r	126.9
Net Change in Consumer Installment Credit †	Nov '87n	$ 2.22	$ 2.88r	$ 0.78
U.S. Merchandise Trade Balance	Nov '87n	–$ 13.22	–$ 17.63	–$ 19.22
Plant and Equipment Expenditures*	1st Q'88	$427.97(a)	$417.25(a)	$372.24
Private Housing Starts (Thousands of Units)*	Nov '87	1,637	1,523	1,637
New Construction Expenditures*	Nov '87n	$ 419.5	$ 410.6r	$ 390.7
Total Business Inventories †	Nov '87n	$ 695.5	$ 689.9r	$ 655.3r
Total Business Sales †	Nov '87n	$ 461.4	$ 462.4r	$ 429.8r

*Seasonally adjusted annual rate. †Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

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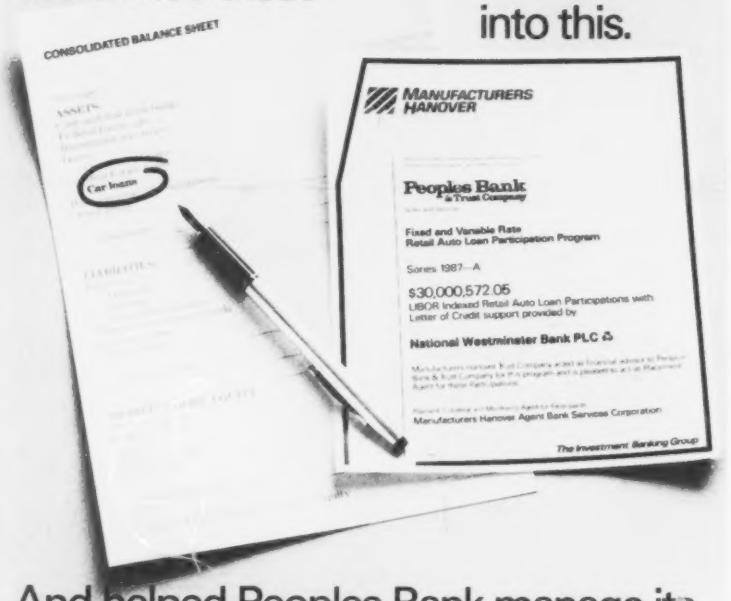
Structured Solutions

We turned these

into this.



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Peoples Bank and Trust, a billion dollar bank located in Rocky Mount, North Carolina, has been very successful in generating profits through new car loans. For Peoples, the challenge was continued loan growth, without constraining its balance sheet.

Manufacturers Hanover Trust responded by packaging and selling Peoples consumer loan receivables. Securitization of these assets enabled Peoples to continue a profitable line of business, retain servicing income and satisfy customer needs.

No matter what type of consumer loans are in your portfolio—car loans, credit card loans, boat loans—Manufacturers Hanover can show you innovative ways to restructure your assets and manage your balance sheet. Call your Manufacturers Hanover relationship manager today for details.

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